

Chapter 1: Executive Summary and Study Overview

This report responds to a request from the Washington State Legislature for the Office of Financial Management (OFM) to undertake a study of local government finances in the context of the Growth Management Act (GMA), with a specific focus on the impact of annexations and incorporations. For the main part of the study, reported in Chapters 2 through 4, a sample of cities and counties in Washington State were selected for inclusion through consultations by Department of Community, Trade and Economic Development (CTED) with the Associations of Washington Cities and Counties. Counties included in this study were Asotin, Clallam, Clark, Pierce, Spokane, and Yakima. Cities included were Asotin, Clarkston, Forks, Port Angeles, Sequim, Battle Ground, Camas, Vancouver, Washougal, Yacolt, Bonney Lake, Puyallup, Steilacoom, Tacoma, University Place, Deer Park, Fairfield, Medical Lake, Spokane, Spokane Valley, Granger, Harrah, Selah, Toppenish, and Yakima.

The cities and counties included in this study have had varied records of annexations and incorporations over the 1994-2003 study time period. This time period was selected because Growth Management Plans were adopted by most of these jurisdictions in about 1994. There are varying reports of impacts of annexations and incorporations on local government finances as a result of this study. Some jurisdictions, such as the City of Yakima and the City of Battle Ground, have grown primarily through annexations, while other jurisdictions have had no growth and no annexations.

Given the limited time and resources for the conduct of the study, it was necessary to draw a sample of counties and cities. We cannot know from this study if its findings are representative of trends in cities and county governments in the other thirty-three counties in Washington State, and in cities located in the case study counties that were not included in this study.

The study brought together public data on local government revenues and expenditures, populations, and annexations and incorporations. The tables and figures in Chapter 3 as well as Appendix I present these data. A key objective of the study was to determine the apparent effect of annexations and incorporations on the finances of local governments included in the study. A general presumption at the outset of the study was that annexations or incorporations would lead to reduced revenues and expenditures of county governments, and to increased revenues and expenditures by city governments. The evidence presented in Chapter 3 indicates that with a few exceptions it is not easy to observe these expected relationships. In the case of very large annexations or incorporations (such as in the City of Vancouver or the City of Spokane Valley), it would be expected that such impacts would be observed. However, in the case of Clark County the framework that allocated service provision by cities to areas inside Urban Growth Boundaries masks such effects. The City of Spokane Valley has been incorporated too recently to allow observation of impacts on Spokane County finances.

Table 32 at the end of Chapter 3 documents the diversity of growth experiences for cities and counties in Washington State, complicating the presumption stated above. This table makes it clear that general government revenues and expenditures have moved as “expected,” and that it is capital and debt related revenues and expenditures that have been the volatile component of local government budgets. Local governments also identified a wide variety of factors associated with their finances, including unfunded state and federal mandates, spillover effects of statewide initiatives, and rising insurance and health care costs. Local government revenues for taxes and services/fees, and spending on general expenditures and utilities have tended to track population change in these local government jurisdictions, including annexations and incorporations. Other revenues and expenditures from capital related revenue sources and expenditures exhibit much more variation, and show little relationship with annexations and incorporations.

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There has not been sufficient detail available regarding these capital and debt related revenues and expenditures to determine their systematic magnitude with respect to annexation and incorporation activity. Table 32 makes it clear that these variations in revenues and expenditures have been observed in both rapidly growing jurisdictions, as well as in those without significant growth.

The survey of local governments reported in Chapter 4 provides confirmation of many of the observations made in Chapter 3. This survey generally finds that annexations have not been a major factor in local government finances, compared to the larger impacts of statewide initiatives such as I-695 that repealed the state motor vehicle excise tax and I-747 that limited growth in property taxes, general population growth, and economic development. This survey found that there were many other contextual factors that were regarded by local governments as more significant impacts on their finances than incorporations and annexations, including unfunded mandates from the state and federal government, additional impacts of statewide initiatives, and the rising costs of factors such as health care for local government employees.

About two-thirds of the jurisdictions are using impact fees as allowed by RCW 82.02, to help pay for growth. Some of the jurisdictions not levying impact fees are considering their adoption. Impact fees are most commonly used for parks, open space, and recreation facilities, school facilities and renovations, and for street and road improvement.

While the general direction of these comments is to suggest that annexations are not important to local government finances, in reality they are important. They must be seen as just one of the factors to be considered in understanding the local government finance picture in Washington State. Jurisdictions such as the City of Yakima, the City of Vancouver, the City of Battle Ground, the City of Spokane Valley, and the City of University Park owe almost all (or all) of their growth to annexations and incorporations. In most cases their revenues (and expenditures) have been dramatically impacted by these land use actions. We have many other communities in which these land use actions have not been important over the study period, but in which there have been significant finance impacts associated with other factors.

A major factor not considered in this study is the way in which local government services and finances are organized in specific jurisdictions. Some cities and counties included in this study provide services, such as electrical power, water, sewer, and other utilities. In other cases these services are provided by special districts (such as water or sewer districts), or private service providers (such as private electrical power providers). These institutional arrangements have a significant impact on the mix and magnitude of local government finance revenues and expenditures. Further research could be undertaken to sort out in these case study communities how these institutional arrangements have been related to their revenues and expenditures, in the context of annexations and incorporations.

This study also contains three chapters that more generally address local government funding. Chapter 5 discusses existing sources of local government tax revenue and any unused capacity for those sources. Chapter 6 briefly summarizes legislation passed by the 2005 Legislature that will provide additional revenues for local governments. Chapter 7 takes a look at a few selected funding mechanisms that other states utilize to fund their local governments.